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In the Supreme Court of the United States

OCTOBER TERM, 1992

PETER E. DUFFY AND NEW ENGLAND INSURANCE COMPANY, PETITIONERS

v.

FEDERAL DEPOSIT INSURANCE CORPORATION, AS MANAGER OF THE FSLIC RESOLUTION FUND, SUBSTITUTED FOR FEDERAL SAVINGS & LOAN INSURANCE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL DEPOSIT INSURANCE CORPORATION IN OPPOSITION

KENNETH W. STARR
Solicitor General
Department of Justice
Washington, D.C. 20530
(202) 514-2217

ALFRED J.T. BYRNE
General Counsel

ANN S. DUROSS
Assistant General Counsel

COLLEEN B. BOMBARDIER
Senior Counsel

JACLYN C. TANER
MARY P. DAVIS
Counsel
Federal Deposit Insurance Corporation
Washington, D.C. 20429

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QUESTION PRESENTED

Whether the court of appeals correctly concluded that the FDIC's settlement of certain malpractice claims against a lawyer and his law firm did not release the FDIC's separate claims against another partner of that same law firm arising out of different malpractice claims.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A14) is reported at 960 F.2d 1325. The relevant district court opinion (Pet. App. A21-A31) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on May 20, 1992, and a petition for rehearing was denied

on June 25, 1992. Pet. App. A54-A55. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The judgment in this case arises from the second of two related cases—"the *Mmahat* case" and "the *Duffy* case"—brought in the United States District Court for the Eastern District of Louisiana. In the *Mmahat* case, the government alleged that John Mmahat and the firm of Mmahat & Duffy (M&D) had committed legal malpractice in their representation of Gulf Federal Savings Bank, a federally insured thrift that had been placed in receivership.[1] Petitioner Peter E. Duffy, the other named partner of Mmahat & Duffy, was *not* a defendant in the *Mmahat* case.

As *Mmahat* proceeded toward trial, the parties agreed to bifurcate the triable issues into "Phase I" claims and "Phase II" claims. The Phase I claims

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[1] The Federal Savings Loan Insurance Corporation (FSLIC) was named receiver of Gulf Federal Savings Bank when the institution was placed in receivership, and the *Mmahat* case was commenced and initially prosecuted by FSLIC in its corporate capacity. Congress abolished FSLIC effective August 9, 1989. Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, § 401, 103 Stat. 354, see 12 U.S.C. 1437 note. Under FIRREA, FSLIC's assets, including the claims at issue in the *Mmahat* and *Duffy* cases, were transferred to the FSLIC Resolution Fund, for which the Federal Deposit Insurance Corporation (FDIC) was appointed manager. Although the parties in the *Mmahat* case continued to refer to the plaintiff as "FSLIC" in the district court proceedings, the FDIC as Manager of the FSLIC Resolution Fund became the litigant in the district court.

were malpractice claims against Mmahat and the law firm based on their advice pertaining to the federal "loans-to-one-borrower" regulation of the Federal Home Loan Bank Board.[2] The Phase I claims were tried and culminated in a $35 million judgment against Mmahat and the law firm. The Fifth Circuit ultimately upheld that judgment, and also affirmed the district court's holding that the $35 million judgment was excluded from coverage pursuant to a dishonesty exclusion in the legal malpractice policy issued by petitioner New England Insurance Company (New England). *FDIC* v. *Mmahat*, 907 F.2d 546 (5th Cir. 1990), cert. denied, 111 S. Ct. 1387 (1991).[3]

The Phase II claims in the *Mmahat* case asserted malpractice with respect to three discrete real estate loan transactions. In December of 1988, after the jury's $35 million verdict against Mmahat and M&D had been announced, but prior to the district court's decision holding that none of that liability was covered by the New England policy, the parties in

[2] An applicable regulation of the Federal Home Loan Bank Board (FHLBB) restricted the amount that a savings and loan could lend to any single borrower. At Mmahat's direction, Gulf Federal violated the regulation on a regular basis, even after receiving warnings from the FHLBB. *FDIC* v. *Mmahat*, 907 F.2d 546, 549 (5th Cir. 1990), cert. denied, 111 S. Ct. 1387 (1991).

[3] New England was named as a defendant in the *Mmahat* case as the insurer of Mmahat and M&D pursuant to Louisiana's Direct Action statute, La. Rev. Stat. Ann. § 22:655 (West Supp. 1992), which allows a plaintiff to join the insurance carrier in its initial action against the insured. New England was later joined as Duffy's malpractice insurer in the *Duffy* case in accordance with that same statute.

Mmahat appeared in the district court to announce their settlement of the Phase II claims for $250,000. The terms of the settlement were read into the record by counsel for the FDIC, speaking on behalf of all of the parties. The district court approved the settlement and dismissed the Phase II claims. However, the parties were later unable to reduce the terms of the oral settlement into a settlement agreement and no signed settlement agreement exists. Pet. App. A3-A4, A11.

2. In December 1989, the FDIC initiated this separate suit against Duffy, and against New England as his insurer, seeking to establish Duffy's individual liability under Louisiana law for his "virile share" of the partnership liability for the Phase I judgment.[4] The FDIC also sought to establish Duffy's status as an "innocent co-insured" whose personal liability was covered by the New England malpractice policy. However, following a hearing on the status of the settlement of the Phase II claims, the district court held that the settlement and release of those claims had also released the FDIC's claims against Duffy for his virile share of the judgment on the Phase I claims. Based on that determination, the district court sua sponte dismissed the FDIC's separate complaint in the *Duffy* case. Pet. App. A21-A31.

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[4] Article 2817 of the Louisiana Civil Code provides that a partnership "as principal obligor is primarily liable for its debts," and that a partner is "bound for his virile share of the debts of the partnership. " La. Civ. Code Ann. art. 2817 (West Supp. 1992). As the court of appeals noted, the number of members in a partnership, rather than the extent of each partner's interest, defines the virile share. Pet. App. A8 n.8.

3. The court of appeals reversed. Pet. App. A1-A14.[5] The court "agree[d] with the FDIC that the district court erred in determining that the FDIC's failure to include *Duffy* as a party to *Mmahat* or mention him in the *Mmahat* pretrial order barred the suit against him." Pet. App. A6. The court explained that implicit in the district court's decision was the conclusion "that Duffy was an indispensable party to the *Mmahat* suit." *Id.* at A7 n.6. But, the court held, "[n]either federal nor Louisiana law requires the joinder of all partners in an action against a partnership." *Id.* at A7. In addition, the court recognized, "[t]he fact that Duffy might have been joined in *Mmahat* does not preclude the FDIC from enforcing the *Mmahat* judgment against Duffy in a separate action." *Id.* at A8.

With respect to the contention that the settlement of the Phase II claims in *Mmahat* barred the FDIC's suit against Duffy, the court first determined that "[w]hen the terms of the settlement are clearly specified in the record, as they are in this case, we

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[5] Duffy, who had filed a voluntary petition in bankruptcy pursuant to Chapter 7 of the Bankruptcy Code (11 U.S.C. 701 *et seq.*) and had been discharged in April of 1990 took no position on the merits of the appeal. Petitioners have noted that Duffy was discharged from any claims "without objection by the FDIC," Pet. 5 n.4, but that assertion is incomplete. Prior to Duffy's discharge, the FDIC sought and obtained an order from the Bankruptcy Court recognizing the FDIC's right to continue to sue Duffy for the purpose of perfecting his liability as a precondition for recovery against petitioner New England as his malpractice carrier. As a result, by the time of the appeal of the *Duffy* case, Duffy had no personal exposure and petitioner New England was the real party in interest.

find it appropriate to use the de novo standard we apply to review written contracts." *Id.* at A6. The court then agreed with the FDIC "that the district court erroneously interpreted the oral settlement agreement as discharging the FDIC's claims against Duffy for his virile share of liability in the judgment against M & D." *Id.* at A10. The court noted that the settlement that was read into the record provided for "[t]he settlement of phase 2 of the litigation"—and not for the settlement of Phase I—and that FDIC's counsel recited that "[t]he FSLIC will settle and grant releases to John Mmahat, Mmahat & Duffy and New England *for the preceding claims*"—*i.e.*, the Phase II claims—"in return for payment of * * * $250,000." *Id.* at A11 (emphasis added by the court of appeals). The court of appeals also noted that the district court faulted the government for failing to reserve any rights against Duffy in the *Mmahat* case. But it concluded that "because Duffy was not a party to the *Mmahat* litigation, the FDIC need not have men-tioned a potential claim against him as an unresolved issue in *Mmahat*." *Id.* at A13.

ARGUMENT

The court of appeals applied settled principles of law in holding that the settlement of *Mmahat* did not bar a separate suit against Duffy, and the court's decision is not in conflict with any decision of this Court or any other court of appeals. Accordingly, further review is not warranted.

1. Petitioners first assert that the court of appeals departed from established principles of appellate review by applying the de novo standard in reviewing the district court's ruling that the settlement in

Mmahat released Duffy. Pet. 9-16. To the contrary, the court of appeals properly applied the standard of review that the Fifth Circuit routinely employs in reviewing written contracts, since the terms of the settlement were "clearly specified in the record." Pet. App. A6, citing *LTV Educ. Sys., Inc.* v. *Bell*, 862 F.2d 1168, 1172 (5th Cir. 1989), and *Weingart* v. *Allen & O'Hara, Inc.*, 654 F.2d 1096, 1103 (5th Cir. 1981). The court recognized that a different standard would apply in cases where the terms of an oral settlement agreement were ambiguous. Pet. App. A6, citing *In re Raymark Indus., Inc.*, 831 F.2d 550, 553 (5th Cir. 1987). There is nothing remarkable or erroneous about the application of the de novo standard to review the terms of an unambiguous statement that is clearly set out in the record reviewed on appeal.

Petitioners devote considerable attention to Rule 52(a) of the Federal Rules of Civil Procedure and to the standard of review that an appellate court should apply in considering a trial court's findings of fact. Pet. 10-16. The principles of Rule 52 are not germane, however. The district court did not find that the settlement agreement was ambiguous, and it did not conduct an evidentiary hearing or receive extrinsic evidence regarding the intent of the settling parties. Nor did the district court purport to make findings of fact or credibility judgments of the kind governed by Rule 52. Rather, the district court interpreted the settlement that had been dictated into the record. The Fifth Circuit's treatment of this issue was correct, and in any event nothing suggests that this issue is worthy of this Court's review.

2. Petitioners also contend that the claim against Duffy was required to be asserted in the *Mmahat* case pursuant to Rule 16 of the Federal Rules of Civil Procedure (which is entitled "Pretrial Conferences; Scheduling; Management") and the district court's pretrial order in the *Mmahat* case. Contrary to petitioners' claim, the court of appeals properly recognized that the district court's reliance on Rule 16 as the governing standard represented an error of law. Rule 16 and the district court's pretrial order do not provide the proper standard for determining whether Duffy should have been joined as a defendant in *Mmahat* or whether the dismissal of *Duffy* was a permissible response to the FDIC's failure to join Duffy in *Mmahat*. Rather, Rule 19 and the general principles of res judicata provide the applicable standards for the resolution of those issues. They protect litigating parties and the interests of absent persons by defining the circumstances in which parties can join or be joined by others, as well as the circumstances in which absent persons must be joined. By contrast, the principles of notice pleading and the discretion afforded the district courts in pretrial procedures supervised pursuant to Rule 16 are applied to assure fairness to the parties participating in the case. Thus, as the court of appeals explained: "Federal Rule of Civil Procedure 16 governs the scope and course of a trial. A court may properly reject an attempt to pursue an issue not contained in the pretrial order unless its consideration is necessary to prevent manifest injustice. However, this rule does not establish whether an

individual must be joined as a *party* to an action." Pet. App. A6-A7 (citations omitted).

The court of appeals also correctly ruled that Duffy was not required to be joined as a defendant in *Mmahat* by Rule 19. Pet. App. A7 n.6. Rule 19 does not require the joinder of joint tortfeasors. See Fed. R. Civ. P. 19, Notes of Advisory Committee on the Amended Rule; see also 7 C. Wright, A. Miller & M. Kane, *Federal Practice and Procedure* § 1623 (2d ed. 1986). Moreover, as the Restatement (Second) of Judgments recognizes, a successful suit against one partner does not terminate the prevailing party's rights against other partners.[6] Applicable Louisiana law is to the same effect. See *Koppers Co. v. Mackie Roofing & Sheet Metal Works*, 544 So.2d 25, 26 (La.

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[6] Section 60 of the Restatement (Second) of Judgments (1982), entitled "Partnerships and its Members," states in pertinent part:

> (1) A judgment in an action by an injured person against a partner upon an obligation or liability incurred in the course of partnership business:
>
> * * * * *
>
> (b) If in favor of the injured person
>
> (i) does not terminate a claim that he may have against another partner based upon that obligation.

See also Restatement (Second) of Judgments § 49 (1982); 59A Am Jur. 2d *Partnership* § 770, at 618 (1987) ("[A]n omission to join partners individually in prior proceedings against a partnership, reducing a partnership debt to judgment, does not prejudice the right to subsequent proceedings at law against the partners individually on the same debt.").

Ct. App. 1989).[7] In sum, the Fifth Circuit's resolution of this issue was correct and requires no further review by this Court.[8]

3. Petitioners also maintain that the court of appeals cannot review de novo a trial court's dismissal entered pursuant to its inherent power to sanction litigants for a suit it deems to have been filed in bad faith. Pet. 20-23. The district court did not find that the *Duffy* case was filed in bad faith, however, nor did it dismiss *Duffy* as a sanction for bad faith conduct. Accordingly, the court of appeals did not consider the district court's dismissal to be one that had been

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[7] In *Koppers*, the plaintiff initially sued the partnership on a contract debt and obtained a judgment against it. The plaintiff then sued the individual partners to recover their virile shares of the partnership liability, and the trial court dismissed the separate suit against the individual partners. Reversing that dismissal, the Louisiana Court of Appeals held that although it might have been more economical for the plaintiff to have proceeded against the partnership and its partners in a single action, Louisiana law allowed the plaintiff to establish the partnership debt in one case and then to proceed separately to establish the individual partners' liability for the partnership obligation. 544 So.2d at 26.

[8] Petitioners also maintain that, because New England was a party to the *Mmahat* litigation in its capacity as insurer for Mmahat and M&D, the FDIC's failure to list in the pretrial order all potential claims that it might have against New England in its capacity as insurer for Duffy bars its assertion of claims against New England in the subsequent *Duffy* suit. Pet. 20. As the court of appeals correctly noted, however, "New England is not an identical party in *Duffy* because the insurance policy provides separate coverage for Duffy as a partner of M&D." Pet. App. A10 n.10. Accordingly, petitioners' contention lacks merit.

entered as a sanction for bad faith litigation, and the petitioners cannot properly raise this issue for the first time in this Court.[9]

4. Finally, petitioners urge the Court to review the Fifth Circuit's observation that the litigation of the *Duffy* case will not require readjudication of the malpractice claim decided in *Mmahat*, since the *Duffy* case is "based on the pre-existing $35 million judgment against Mmahat and M&D and Duffy's virile share of liability for that debt pursuant to Louisiana Civil Code Article 2817." Pet. App. A9.[10] Pet. 28-30. Petitioners assert that the "Fifth Circuit's dictum that relitigation would not be required was in error." *Id.* at 28.

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[9] None of the authorities advanced by petitioners in support of this contention were even cited by New England in its brief in the court of appeals, and Duffy did not file a brief on the merits in the court below.

[10] The court of appeals offered that observation in response to petitioner New England's mistaken arguments that the "claims" at issue in *Duffy* were the same as those adjudicated in *Mmahat* and that res judicata required Duffy to be joined in *Mmahat* or not be sued at all. Pet. App. A9. As the Fifth Circuit responded (*ibid.*):

> *Duffy* does not rest on an identical obligation, nor does it require readjudication of the malpractice claim. *Mmahat* was based on the malpractice of Mmahat, committed as a partner of the firm. In contrast, *Duffy* is based on the pre-existing $35 million judgment against Mmahat and M&D and Duffy's virile share of liability for that debt pursuant to Louisiana Civil Code Article 2817. Thus, the FDIC did not pursue a new theory of recovery in *Duffy*; it sought merely to collect a pre-existing judgment in its favor.

Although petitioners stray from the mark in suggesting that the court of appeals' statement is pure dictum, petitioners' characterization demonstrates that the question that they offer for this Court's consideration is not properly presented by this judgment. Although the FDIC believes that many of the points that petitioners might wish to relitigate in *Duffy* will indeed be foreclosed by principles of collateral estoppel,[11] the fact remains that the collateral estoppel effect of *Mmahat* on issues to be tried in *Duffy* has not yet been decided and is not ripe for this Court's consideration. Petitioners will be free in *Duffy* to urge every position on this question they advocate to this Court when *Duffy* proceeds to trial in the district court.

[11] For example, the Restatement (Second) of Judgments provides that a judgment in favor of a plaintiff against one partner can have binding collateral estoppel effect against another partner in subsequent litigation if the second partner "was given notice of an opportunity to defend" in the first action. Restatement (Second) of Judgments § 60(1)(b)(ii) (1982). The FDIC believes that the record will establish that Duffy received such notice. Thus, collateral estoppel will preclude relitigation of certain issues decided in *Mmahat*, such as Mmahat's malpractice and the responsibility of Mmahat & Duffy for that malpractice.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

KENNETH W. STARR
Solicitor General

ALFRED J.T. BYRNE
General Counsel

ANN S. DUROSS
Assistant General Counsel

COLLEEN B. BOMBARDIER
Senior Counsel

JACLYN C. TANER
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